SIMPLE IRA Plan Checklist

DO NOT FILE WITH IRS

Every year it is important to review the requirements for operating your SIMPLE IRA plan. This SIMPLE IRA Plan Checklist has been designed as a quick diagnostic tool to help you keep your SIMPLE IRA plan in compliance with important tax rules. This SIMPLE IRA Plan Checklist is not a complete description of all the requirements and it is not a substitute for a comprehensive plan review.

Use of this SIMPLE IRA Plan Checklist is voluntary. **YES NO**

1. Does your business have 100 employees or less? ☐ ☐
   (Businesses with more than 100 employees - including full-time, part-time, and seasonal employees – who earned at least $5,000 cannot establish a SIMPLE IRA plan.)

2. Is this SIMPLE IRA plan your business's only employee retirement plan? ☐ ☐
   (A sponsor of a SIMPLE IRA plan generally cannot sponsor any other retirement plan, such as a 401(k) plan.)

3. Have you identified all of your eligible employees? ☐ ☐
   (Any employee with at least $5,000 in compensation in 2 prior years and is expected to earn at least $5,000 this year is eligible to participate in a SIMPLE IRA plan.)

4. Did you notify your eligible employees of their right to elect salary reduction or to modify a prior salary reduction agreement? ☐ ☐
   (Employees must be given notice before November 2 each year of their right to participate in the plan in the next year or change a prior salary reduction agreement.)

5. Have you given all of your eligible employees a copy of the SIMPLE IRA plan agreement (Form 5304-SIMPLE or Form 5305-SIMPLE, if you use the model forms)? ☐ ☐
   (Instead, you can give your employees a "summary description." This document must describe the basic features of the plan, information about the employer and trustee, eligibility requirements, etc.)

6. If you changed your plan, did you give your employees notice of any changes before November 2 for changes taking effect in the following calendar year? ☐ ☐
   (Employees must be given notice of any plan changes at least 60 days prior to the start of the next calendar year.)

7. Have you allowed employees to terminate their salary reduction election? ☐ ☐
   (Employees must be allowed to stop making deferrals at any time.)

8. Have you deposited employee deferrals timely? ☐ ☐
   (Employee deferrals (amounts that employees elect to contribute by salary reduction) must be deposited in the IRA as soon as possible but in no event later than 30 days following the month in which the employee would have otherwise received the money.)

9. Did you timely deposit the required employer contributions into the SIMPLE IRAs? ☐ ☐
   (Employers have until the due date – including extensions – of their tax return for the tax year that includes the last day of the calendar plan year to deposit matching contributions or employee deferrals.)

10. Are employee deferrals to SIMPLE IRAs limited as required by law? ☐ ☐
    (The contribution limit to a SIMPLE IRA is $8,000 in 2003, $9,000 in 2004, and $10,000 in 2005. Catch-up contributions for participants aged 50 or over are limited to an additional $1,000 in 2003, $1,500 in 2004, and $2,000 in 2005.)

If you answered "No" to any of the above questions, you may have made a mistake in operating your SIMPLE IRA plan. Many mistakes can be corrected easily, without penalty and without notifying the IRS. We suggest that you contact your benefits professional. For more information, visit the IRS Retirement Plans web page at www.irs.gov/ep or call IRS TE/GE Customer Account Services toll-free at 1-877-829-5500.

SIMPLE IRA Plan

A savings incentive match plan for employees (SIMPLE plan) is a written arrangement that provides you and your employees with a simplified way to make contributions to provide retirement income. Under a SIMPLE plan, employees can choose to make salary reduction contributions to the plan rather than receiving these amounts as part of their regular pay. In addition, you will contribute matching or nonelective contributions.

A SIMPLE IRA plan uses SIMPLE IRAs that are set up for each eligible employee.

Credit for startup costs: You may be able to claim a tax credit for part of the ordinary and necessary costs of starting a SIMPLE IRA plan that first became effective in 2002.

Deadline for setting up a SIMPLE IRA plan: You can set up a SIMPLE IRA plan effective on any date between January 1 and October 1 of a year, provided you did not previously maintain a SIMPLE IRA plan. This requirement does not apply if you are a new employer that comes into existence after October 1 of the year the SIMPLE IRA plan is set up and you set up a SIMPLE IRA plan as soon as administratively feasible after you come into existence. If you previously maintained a SIMPLE IRA plan, you can set up a SIMPLE IRA plan effective only on January 1 of a year. A SIMPLE IRA plan cannot have an effective date that is before the date you actually adopt the plan.

Setting up a SIMPLE IRA: SIMPLE IRAs are the individual retirement accounts or annuities into which the contributions are deposited. A SIMPLE IRA must be set up for each eligible employee. *Forms 5305–S*, *SIMPLE Individual Retirement Trust Account,* and *5305–SA*, *SIMPLE Individual Retirement Custodial Account,* are model trust and custodial account documents the participant and the trustee (or custodian) can use for this purpose.

You can use *Form 5304–SIMPLE* or *Form 5305–SIMPLE* to set up a SIMPLE IRA plan. Each form is a model savings incentive match plan for employees (SIMPLE) plan document. Which form you use depends on whether you select a financial institution or your employees select the institution that will receive the contributions.

Use Form 5304–SIMPLE if you allow each plan participant to select the financial institution for receiving his or her SIMPLE IRA plan contributions. Use Form 5305–SIMPLE if you require that all contributions under the SIMPLE IRA plan be deposited initially at a designated financial institution.

The SIMPLE IRA plan is adopted when you have completed all appropriate boxes and blanks on the form and you (and the designated financial institution, if any) have signed it. Keep the original form. Do not file it with the IRS.

Other uses of the forms: If you set up a SIMPLE IRA plan using Form 5304–SIMPLE or Form 5305–SIMPLE, you can use the form to satisfy other requirements, including the following:

- Meeting employer notification requirements for the SIMPLE IRA plan. Page 3 of Form 5304–SIMPLE and Page 3 of Form 5305–SIMPLE contain a *Model Notification to Eligible Employees* that provides the necessary information to the employee.
- Maintaining the SIMPLE IRA plan records and proving you set up a SIMPLE IRA plan for employees.

A SIMPLE IRA cannot be designated as a Roth IRA. Contributions to a SIMPLE IRA will not affect the amount an individual can contribute to a Roth IRA.

Deadline for setting up a SIMPLE IRA: A SIMPLE IRA must be set up for an employee before the first date by which a contribution is required to be deposited into the employee's IRA. See *Time limits for contributing funds,* later.

SIMPLE IRA plans can only be maintained on a calendar-year basis.

TIP: *Many financial institutions will help you set up a SIMPLE plan.*

1) 100-Employee Limit

You can set up a SIMPLE IRA plan only if you had 100 or fewer employees who received $5,000 or more in compensation from you for the preceding year. Under this rule, you must take into account ***all*** employees employed at any time during the calendar year regardless of whether they are eligible to participate. Employees include self-employed individuals who received earned income and leased employees.

Once you set up a SIMPLE IRA plan, you must continue to meet the 100-employee limit each year you maintain the plan.

Grace period for employers who cease to meet the 100-employee limit: If you maintain the SIMPLE IRA plan for at least 1 year and you cease to meet the 100-employee limit in a later year, you will be treated as meeting it for the 2 calendar years immediately following the calendar year for which you last met it.

A different rule applies if you do not meet the 100-employee limit because of an acquisition, disposition, or similar transaction. Under this rule, the SIMPLE IRA plan will be treated as meeting the 100-employee limit for the year of the transaction and the 2 following years if both the following conditions are satisfied:

- Coverage under the plan has not significantly changed during the grace period.
- The SIMPLE IRA plan would have continued to qualify after the transaction if you had remained a separate employer.

The grace period for acquisitions, dispositions, and similar transactions also applies if, because of these types of transactions, you do not meet the rules explained under *Only Retirement Plan* or *Eligible Employees*, below.

2) Only Retirement Plan

The SIMPLE IRA plan generally must be the only retirement plan to which you make contributions, or to which benefits accrue, for service in any year beginning with the year the SIMPLE IRA plan becomes effective.

Exception: If you maintain a qualified plan for collective bargaining employees, you are permitted to maintain a SIMPLE IRA plan for other employees.

3) Eligible Employees

Any employee who received at least $5,000 in compensation during any 2 years preceding the current calendar year and is reasonably expected to receive at least $5,000 during the current calendar year is eligible to participate. The term “employee” includes a self-employed individual who received earned income.

You can use less restrictive eligibility requirements (but not more restrictive ones) by eliminating or reducing the prior year compensation requirements, the current year compensation requirements, or both.

For example, you can allow participation for employees who received at least $3,000 in compensation during any preceding calendar year. However, you cannot impose any other conditions for participating in a SIMPLE IRA plan.

Excludable employees: The following employees do not need to be covered under a SIMPLE IRA plan:

- Employees who are covered by a union agreement and whose retirement benefits were bargained for in good faith by the employees’ union and you.
- Nonresident alien employees who have received no U.S. source wages, salaries, or other personal services compensation from you.

4&6) Notification Requirements

You must notify each employee of the following information before the beginning of the election period:

1) The employee's opportunity to make or change a salary reduction choice under a SIMPLE IRA plan.
2) Your choice to make either matching contributions or nonelective contributions (discussed later).
3) A summary description and the location of the plan. The financial institution should provide you with this information.
4) Written notice that his or her balance can be transferred without cost or penalty if you use a designated financial institution.

Election period: The election period is generally the 60-day period immediately preceding January 1 of a calendar year (November 2 to December 31 of the preceding calendar year). However, the dates of this period are modified if you set up a SIMPLE IRA plan in mid-year (for example, on July 1) or if the 60-day period falls before the first day an employee becomes eligible to participate in the SIMPLE IRA plan. A SIMPLE IRA plan can provide longer periods for permitting employees to enter into salary reduction agreements or to modify prior agreements. For example, a SIMPLE IRA plan can provide a 90-day election period instead of the 60-day period. Similarly, in addition to the 60-day period, a SIMPLE IRA plan can provide quarterly election periods during the 30 days before each calendar quarter, other than the first quarter of each year.

5) Copy of the Plan

You must give all of your eligible employees a copy of the SIMPLE IRA plan agreement. If you use one of the model forms (Form 5304-SIMPLE or Form 5305-SIMPLE), the form is your SIMPLE IRA plan agreement. In lieu of a copy of the SIMPLE IRA plan agreement, you can give your eligible employees a "summary description" of your SIMPLE IRA plan agreement. The summary description must describe the basic features of the plan, information about the employer, trustee, eligibility requirements, etc.

7) Notification Requirements: Stopping Deferrals

You must notify each employee of their right to stop – at any time – making their salary reduction deferrals.

8) Depositing Employee Deferrals

Employee deferrals are amounts that employees elect to contribute to the SIMPLE IRA plan by salary reduction. In accordance with Department of Labor ("DOL") rules, an employer must forward employee contributions to the financial institution as soon as they can reasonably be segregated from the employer's general assets, but in no event later than 30 days following the month in which they were withheld from the employee's paycheck. For more information on the DOL rules, go to their web site at www.dol.gov/ebsa.

9) Depositing Employer Contributions

An employer's matching or nonelective contributions must be made to the selected financial institution no later than the due date for filing the employer's tax return (including extensions) for the employer's tax year with or within which the calendar year for which the contribution was made ends.

10) Contribution Limits

Contributions are made up of salary reduction contributions and employer contributions. You, as the employer, must make either matching contributions or nonelective contributions, defined later. No other contributions can be made to the SIMPLE IRA plan. These contributions, which you can deduct, must be made timely. See *Depositing Employee Deferrals* and *Depositing Employer Contributions* above.

Salary reduction contributions: The amount the employee chooses to have you contribute to a SIMPLE IRA on his or her behalf cannot be more than $8,000 for 2003 ($9,000 for 2004). These contributions must be expressed as a percentage of the employee's compensation unless you permit the employee to express them as a specific dollar amount. You cannot place restrictions on the contribution amount (such as limiting the contribution percentage), except to comply with this dollar limit.

If an employee is a participant in any other employer plan during the year and has elective salary reductions or deferred compensation under those plans, the salary reduction contributions under a SIMPLE IRA plan also are elective deferrals that count toward the overall annual limit ($12,000 for 2003, $13,000 for 2004) on exclusion of salary reductions and other elective deferrals.

Catch-up contributions: A SIMPLE IRA plan can permit participants who are age 50 or over at the end of the calendar year to also make catch-up contributions. The catch-up contribution limit for 2003 is $1,000 ($1,500 for 2004). Salary reduction contributions are not treated as catch-up contributions for 2003 until they exceed $8,000. However, the catch-up contribution a participant can make for a year cannot exceed the lesser of the following amounts:

- The catch-up contribution limit.
- The excess of the participant's compensation over the salary reduction contributions that are not catch-up contributions.

Employer matching contributions: You are generally required to match each employee's salary reduction contributions on a dollar-for-dollar basis up to 3% of the employee's compensation. This requirement does not apply if you make nonelective contributions as discussed later.

Lower percentage: If you choose a matching contribution less than 3%, the percentage must be at least 1%. You must notify the employees of the lower match within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year. You cannot choose a percentage less than 3% for more than 2 years during the 5-year period that ends with (and includes) the year for which the choice is effective.

Nonelective contributions: Instead of matching contributions, you can choose to make nonelective contributions of 2% of compensation on behalf of each eligible employee who has at least $5,000 (or some lower amount you select) of compensation from you for the year. If you make this choice, you must make nonelective contributions whether or not the employee chooses to make salary reduction contributions.

For 2003, only $200,000 of the employee's compensation can be taken into account to figure the contribution limit. In 2004, the limit is $205,000.

If you choose this 2% contribution formula, you must notify the employees within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year.

When to Deduct Contributions

You can deduct SIMPLE IRA contributions in the tax year with or within which the calendar year for which contributions were made ends. You can deduct contributions for a particular tax year if they are made for that tax year and are made by the due date (including extensions) of your federal income tax return for that year.

Example 1. Your tax year is the fiscal year ending June 30. Contributions under a SIMPLE IRA plan for the calendar year 2003 (including contributions made in 2003 before July 1, 2003) are deductible in the tax year ending June 30, 2004.

Example 2. You are a sole proprietor whose tax year is the calendar year. Contributions under a SIMPLE IRA plan for the calendar year 2003 (including contributions made in 2004 by April 15, 2004) are deductible in the 2003 tax year.

Where to Deduct Contributions

Deduct the contributions you make for your common-law employees on your tax return. For example, sole proprietors deduct them on Schedule C (Form 1040), *Profit or Loss From Business,* or Schedule F (Form 1040), *Profit or Loss From Farming,* partnerships deduct them on Form 1065, *U.S. Return of Partnership Income,* and corporations deduct them on Form 1120, *U.S. Corporation Income Tax Return,* Form 1120–

A, *U.S. Corporation Short-Form Income Tax Return,* or Form 1120S, *U.S. Income Tax Return for an S Corporation.*

Sole proprietors and partners deduct contributions for themselves on line 30 of the 2003 Form 1040, *U.S. Individual Income Tax Return.* (If you are a partner, contributions for yourself are shown on the Schedule K-1 (Form 1065), *Partner's Share of Income, Credits, Deductions, etc.,* you get from the partnership.)

Tax Treatment of Contributions

You can deduct your contributions and your employees can exclude these contributions from their gross income. SIMPLE IRA contributions are not subject to federal income tax withholding. However, salary reduction contributions are subject to social security, Medicare, and federal unemployment (FUTA) taxes. Matching and nonelective contributions are not subject to these taxes.

Reporting on Form W–2: Do not include SIMPLE IRA contributions in the "Wages, tips, other compensation box" of Form W–2. However, salary reduction contributions must be included in the boxes for social security and Medicare wages. Also include the proper code in box 12. For more information, see the instructions for Forms W–2 and W–3.